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Supreme Court, U.S.
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No. 86-

IN THE

Supreme Court of the United States

October Term, 1986

CANISIUS COLLEGE,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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10 pp

QUESTIONS PRESENTED

1. Whether alleged "curative legislation" which represents a change in prior legislative policy can be relied upon to extinguish vested rights which existed before the passage of the alleged "curative legislation."

2. Whether a court can supply words to a statute to give the statute meaning which it lacks on its face.

3. Whether a revenue ruling that is contrary to clear Congressional intent can be used to defeat that intent.

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STATUTES INVOLVED

Section 3121(a)(2)(A) of the Internal Revenue Code of 1954, as amended, 26 U.S.C. §3121(a)(2)(A), during the period at issue provided in relevant part:

> (a) Wages. — For purposes of this chapter, the term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash; except that such term shall not include —
>
> * * * * *
>
> (2) the amount of any payment (including any amount paid by an employer for insurance or annuities, or into a fund, to provide for any such payment) made to, or on behalf of, any employee or any of his dependents under a plan or system established by an employer which makes provision for his employees generally (or for his employees generally and their dependents) or for a class or classes of his employees (or for a class or classes of his employees and their dependents), on account of —
>
> (A) retirement,

Section 1426(a)(2) of the Internal Revenue Code of 1939, enacted as part of the Social Security Act Amendments of 1939, P.L. 76-379, 53 Stat. 1360, 1373 (1939), provided in relevant part:

> (a) Wages. — The term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash; except that such term shall not include —
>
> * * * * *
>
> (2) the amount of any payment made to, or on behalf of, an employee under a plan or system established by an employer which makes provision for his employees generally or for a class or classes of his employees (including any amount paid by an employer for insurance or annuities, or into a fund, to provide for any such payment), on account of (A) retirement, or (B) sickness or accident disability, or (C) medical and hospitalization expenses in connection with sickness or accident disability, or (D) death, provided the employee (i) has not the option to receive, instead of provision for such death benefit, any part of such payment, or, if such death benefit is insured, any part of the premiums (or contributions to premiums) paid by his employer, and (ii) has not the right, under the provisions of the plan or system or policy of insurance providing for such death benefit, to assign such benefit, or to receive a cash consideration in lieu of such benefit either upon his withdrawal from the plan or system providing for such benefit or upon termination of such plan or system or policy of insurance or of his employment with such employer.

Section 3121(a)(5)(D)[1] of the Internal Revenue Code of 1954, enacted in Section 324(a)(2) of the Social Security Amendments of 1983, P.L. 98-21, 97 Stat. 65, 122 (1983), provides in relevant part:

> (a) Wages. — For purposes of this chapter, the term "wages" means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash; except that such term shall not include —
>
> * * * * *
>
> (5) any payment made to, or on behalf of, an employee or his beneficiary —
>
> * * * * *
>
> (E) under or to an annuity contract described in Section 403(b), other than a payment for the purchase of such contract which is made by reason of a salary reduction agreement (whether evidenced by a written instrument or otherwise)

Section 324(d)(1) of the Social Security Amendments of 1983, P.L. 98-21, 97 Stat. 65, 125 (1983), provides:

> Except as otherwise provided in this subsection, the amendments made by this section shall apply to remuneration paid after December 31, 1983.

---

1. Section 3121(a)(5)(D) was enacted in 1983 as Section 3121(a)(5)(E). The 1984 amendments relettered Section 3121(a)(5)(E) as Section 3121(a)(5)(D) because Section 3121(a)(5)(C) was repealed as obsolete. To avoid confusion, the provision will be referred to as Section 3121(a)(5)(D) throughout.

Section 327 of the Social Security Amendments of 1983, P.L. 98-21, 97 Stat. 65, 127 (1983), codified in 26 U.S.C. §3121(a), provides in relevant part:

> (b)(1) Nothing in the regulations prescribed for purposes of chapter 24 (relating to income tax withholding) which provides an exclusion from "wages" as used in such chapter shall be construed to require a similar exclusion from "wages" in the regulations prescribed for purposes of this chapter.
>
> * * * * *
>
> (d)(1) Except as provided in paragraph (2), the amendments made by subsections (a) and (b) shall apply to remuneration paid after December 31, 1983.

Section 266?(g) of the Deficit Reduction Act of 1984, P.L. 98-369, 98 Stat. 494, 1160 (1984), provides in relevant part:

> Section 327(d) of such Amendments (relating to codification of *Rowan* decision with respect to meals and lodging) is amended to read as follows:
>
> * * * * *
>
> (2) The amendments made by subsection (b) and subsection (c)(4) shall apply to remuneration . . . paid after March 4, 1983, and to any such remuneration paid on or before such date which the employer treated as wages when paid.

No. 86-

IN THE
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October Term, 1986

CANISIUS COLLEGE,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Petitioner, Canisius College, hereby prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit in this matter and in support thereof states the following.

DECISIONS BELOW

The opinion of the District Court, No. 84-1126E, slip op. (W.D.N.Y. March 10, 1986) is not officially reported. It appears in the Appendix hereto at A46. The opinion of the Court of Appeals, reported at 799 F.2d 18 (2d Cir. 1986), appears in the Appendix hereto at A1.

STATEMENT OF JURISDICTION

The judgment of the Court of Appeals (No. 86-6065) issued on August 20, 1986. Justice Marshall issued an order granting petitioner until January 17, 1987 to file this petition for certiorari. This Court has jurisdiction under 28 U.S.C. §1254(1).

STATEMENT OF THE CASE

A. THE PARTIES

Petitioner Canisius College ("Canisius" or "Petitioner") is a non-profit educational organization described in Section 501(c)(3) of the Internal Revenue Code of 1954, as amended (the "Code"), and exempt from Federal income tax under Section 501(a) of the Code.

Respondent is the United States of America.

B. FACTS

The facts are not in dispute. The District Court summarized the facts as follows:

"Canisius is a non-profit educational institution exempt from federal income tax pursuant to section 501(c)(3)

of the Internal Revenue Code. In 1980 Canisius had in effect an employee retirement annuity plan of a type described in 28 U.S.C. Section 403(b). Under such plan certain employees agreed to accept wage reductions in exchange for Canisius' purchase of annuity contracts on their behalves. Pursuant to section 403(b), the cost or value of the contracts was excludable from the employees' 1980 gross income for federal withholding tax purposes. No question appears to exist concerning Canisius' eligibility to develop or implement such a plan or concerning the propriety of excluding the cost or value of the annuities from the participating employees' gross income for federal income tax withholding purposes.

"In contrast to the treatment of such employer contributions for income tax purposes, the amounts used to purchase annuities had been declared in Revenue Ruling 65-208, 1965-2 Cum. Bull. 383, to be includable in the FICA wage base. In compliance with such ruling, Canisius withheld taxes from its employees' wages based upon such inclusion. Canisius also paid the corresponding FICA taxes imposed on it as an employer as measured by the FICA taxable wage bases of its employees.

"In 1981 the United States Supreme Court decided Rowan Cos. v. United States ("Rowan"), 452 U.S. 247, which held that "wages" must be consistently interpreted for federal income withholding and for FICA purposes. Id. at 263.

"In light of such holding, Canisius sought the refund of employer and employee FICA taxes for the 1980 tax year together with statutory interest on behalf of itself and a number of its employees who had participated in the salary reduction annuity plan. In a letter dated April 30, 1984 the Director of the Massachusetts Service Center of the Internal Revenue Service notified Canisius that the refund request had been disallowed in full based upon Revenue Ruling 65-208." (A47). Thereafter the suit below was initiated.

1. Section 403(b) Annuities

Section 403(b) of the Internal Revenue Code of 1954, as amended, ("Code") [26 U.S.C. 403(b)] creates a tax exclusion on all amounts "contri-

buted by the employer" to the annuity plan. An amount is considered "contributed by the employer" if the amount is (a) in addition to the employee's regular salary, or (b) in lieu of a portion of the employee's salary pursuant to a salary reduction agreement. Consequently, as dictated by its legislative history Section 403(b) makes no distinction between the salary reduction portion of the cost of an annuity and the salary supplement portion as they are treated as employer contributions excludable from the employee's taxable income. See Treasury Regulation Section 1.403(b)-1(b) (3) (i), 26 C.F.R. Section 1.403(b)-1(b) (3) (i).

The Internal Revenue Service agrees that these employer contributions for

the purchase of Section 403(b) annuities are not "wages" for income tax withholding purposes. However, the I.R.S. also takes the position that any salary reduction portion of an employer contribution for the purchase of a Section 403(b) annuity is to be considered "wages" for FICA purposes. Revenue Ruling 65-208, 1965-2 C.B. 383. This position is contrary to the definition of wages in Section 3121 of the Code and clear Congressional intent dating back to 1939.[2]

---

2. Pursuant to Section 3121(a) (2) of the Code and its predecessor sections the term "wages" excluded payments to these tax-sheltered annuities from taxes under the Federal Insurance Contributions Act ("FICA") 26 U.S.C. Section 3101 et. seq. See Section 1426 of the Internal Revenue Code of 1939, Social Security Act Amendments of 1939, P.L. 76-379, §201 53 Stat. 1360, 1373 (1939).

2. The Rowan Decision

In Rowan Companies, Inc. v. United States, 252 U.S. 247 (1981), this Court found that the plain language and legislative history of the enactment of the definition of wages for FICA, FUTA [Federal Unemployment Tax Act ("FUTA"), 26 U.S.C. Section 3301, et. seq.] and income tax withholding purposes showed that Congress intended that each mean the same thing. The Court stated, at 252 U.S. 257: "[I]t would be extraordinary for a Congress pursuing this interest . . . (of coordinating the income-tax withholding system with FICA and FUTA) . . . to intend, without ever saying so, for identical definitions to be interpreted differently." Rather, "[T]he plain language and legislative histories of the revelant Acts indicate

that Congress intended its definition to be interpreted in the same manner to FICA and FUTA as for income-tax withholding."

3. Congress and the Rowan Decision

The Conference Report of the Social Security Amendments of 1983 (P.L. 98-21) acknowledged that the "present law" (as of March 4, 1983) provided that these contributions were FICA tax exempt. The report states:

> "Subject to certain limitations, amounts paid by the employer for the purchase of a tax-sheltered annuity for an eligible employee are excluded from the employee's taxable income and social security wage base. Tax-sheltered annuities may be purchased for employees of educational institutions and certain tax-exempt organizations. Tax-sheltered annuities may be purchased pursuant to a salary reduction agreement." (Emphasis added). (House Conference Rep. No. 98-47,

98th Cong., 1st Sess. 146 (1983), reprinted in U.S. Code Cong. & Ad. News, May 1983, Vol. 2 p. 436.)

The subsequent actions of Congress conclusively show that it considered Revenue Ruling 65-208 overruled by the Rowan decision.

Congress did two relevant things in the 1983 Social Security Amendments: First it changed the definition of wages subject to FICA tax to include retirement plans and contributions funded through salary reduction agreements P.L. 98-21, Section 324(a) (2), adding 26 U.S.C. 3121(a) (5) (E) now 26 U.S.C. Section 3121(a) (5) (D); second, in direct response to the variance in the definition of "wages" found prohibitive by Rowan, Section 328(b) (1) of the Amendments added language which allowed

the I.R.S. to interpret "wages" for income tax purposes differently from "wages" for FICA purposes. The provision states:

> "Nothing in the regulations prescribed for purposes of chapter 24 (relating to income tax withholding) which provides an exclusion from 'wages' as used in such chapter shall be construed to require a similar exclusion from 'wages' in the regulations prescribed for purposes of this chapter." (Codification is found following Section 3121(a) (20) of the Code.) (The "Rowan decoupling provision")

As a result of the passage of the 1983 legislation, such remuneration paid after December 31, 1983 became taxable for FICA purposes.

The Deficit Reduction Act of 1984, P.L. 98-369, Section 2662(g), 98 Stat. 494, 1160, amended the 1983 Act by changing the effective date of the Rowan

decoupling provision to "apply to remuneration...paid after March 4, 1983, and to any such remuneration paid on or before such date which the employer treated as wages when paid."

The Supplemental Report of the House Committee on Ways and Means explains that the provision contained in the Deficit Reduction Act of 1984 "prevents the application to compensation, other than meals and lodging, of the Supreme Court's reasoning in Rowan Companies, Inc. v. United States, 452 U.S. 247 (1981)."

It is not disputed, nor can it be, that the change in the definition of "wages" contained in the 1983 Amendments was not made retroactive by the 1984 Congress. Indeed, the majority in Temple University v. United States of

America, 769 F.2d 126, 131 (3rd Cir. 1985) cert. denied, 106 S. Ct. 2914, ___ U.S. ____ (1986) acknowledges this.

Judge Weis states in his dissent in Temple at 137:

> "Despite what was said in the Committee reports, the legislation passed in 1984 did not change the effective date of the definition of wages as modified in 1983. Because the relevant exclusion from the FICA definition of wages between 1939 and 1983 was not altered by statute, the amended definition does not apply to the period at issue here -- 1979-1982."

The committee report continues:

> "The provision in the...(1983 Social Security)...Amendments applies to remuneration paid after December 31, 1983, for FICA and social security benefit purposes and to remuneration paid after December 31, 1984, for FUTA purposes. Thus, it is possible that this provision could be cited as demonstrating Congressional intent that the reasoning of the Rowan decision should generally apply before these

> dates to types of remuneration other than meals and lodging excluded under Section 119, e.g., to contributions under a salary reduction agreement to tax-sheltered annuities (Sec. 403(b))." (House Report No. 98-432, Part II 98th Cong., 2nd Sess. pp. 1657-58 (1984) reprinted in U.S. Code Cong. & Ad. News, August 1984, Vol. 6B p. 586).

Thus, Congress changed the effective date of the Rowan decoupling provision to apply retroactively to all remuneration paid before or after March 4, 1983 which the employer treated as wages when paid. The Committee report states:

> "In order to avoid the inferences which this provision could raise, the bill clarifies the effective date of the provision overriding the Rowan decision so that the provision applies for all purposes, other than the treatment of certain employer-provided meals and lodging, both to remuneration paid after March 4, 1983, and to remuneration paid on or before

> March 4, 1983, which the employer treated as wages when paid..." (Emphasis added.) (Ibid.)

C. PROCEEDINGS IN THE DISTRICT COURT

Following denial of its refund claim by the District Director of the Internal Revenue Service, Canisius brought this action in the United States District Court for the Western District of New York, invoking jurisdiction under 28 U.S.C. § 1346(a)(1), 28 U.S.C. § 1331(a), and 28 U.S.C. § 1340. Upon cross-motions for summary judgment, the district court held that "it is inappropriate to attempt to legitimatize Revenue Ruling 65-208 based upon the financial state of the national system of social insurance in 1965, 1983 or 1984 or upon Congress' 1983 and 1984 debates, reports and enactments amending

the relevant law. It is therefore found that Revenue Ruling 65-208 did not validly reflect the plain language, origin or purpose of section 3121(a)." (A50). However the Court also found that the 1983 and 1984 legislation effectively cut off plaintiff's rights to refunds.

D. PROCEEDINGS IN THE COURT OF APPEALS

Upon appeal the Court of Appeals affirmed the district court. "Even if 65-208 were to be viewed as not in conflict with a specific statutory exclusion from FICA wages, it would nonetheless be contrary to Rowan. For it included an amount in FICA wages that was not included in wages for income-tax withholding purposes and was thus inconsistent with the Rowan requirement of parallel treatment of wages for FICA

and income-tax purposes." (A17 - A18). However, the Court found that Congress, by the 1983 and 1984 legislation had effectively taken away Canisius College's rights to refunds notwithstanding that the language of the legislation did not make the new definition of wages for FICA tax purposes retroactive. Thus, even though at all times the definition of wages for FICA tax purposes excluded the sums which formed the basis of the refund request and suit, the Court held that petitioner had no vested right to a refund.

REASONS FOR GRANTING THE WRIT

I. INTRODUCTION

Petitioner requests that the writ be granted for the following reasons:

A. The fundamental obligation of the government to follow established law and deal fairly with its citizens is presented here. The Court below expressly found that there was no basis in law for the collection of the taxes herein, both because Revenue 65-208 was contrary to existing congressional intent, and also because of the Rowan decision. Yet the Court then sanctioned the retroactive change in near half century old legislative policy which resulted in retroactive overruling of a

decision of this Court under the guise of "curative legislation" to bar the refunds and stripped the petitioner of its vested rights. This action is particularly troublesome and unfair because at the time that the refund request was made and denied it is clear that under the then-existing law the refunds were due. The government disregarded the law and refused to pay refunds. It should be estopped from benefiting from its unlawful conduct of refusing to follow the law and ordered to pay the refunds.

B. There is a conflict between the Third Circuit on the one hand and the First and Second Circuits on the other regarding the weight to

be given to a revenue ruling when the express legislative history of the relevant statute is contrary to the revenue ruling.

II. THIS COURT SHOULD GRANT CERTIORARI TO REESTABLISH THAT CONGRESS CANNOT EXTINGUISH VESTED RIGHTS UNDER THE GUISE OF "CURATIVE LEGISLATION."

The Court below found that although there was no basis for the collection of the tax herein, Congress' action in 1984 constituted "curative legislation" which did not take away any vested right of the taxpayer. This is wrong.

This action by Congress is not permissible curative legislation. Justice White's dissent in the denial of certiorari in Van Emmerik v. Janklow, 454 U.S. 1131, 1132, 102 S.Ct. 986, 987, 71 L.Ed. 2d 285, 286 (1982), quotes United States v. Heinszen & Co., 206 U.S. 370, 374:

> . . . the legislature may 'cure irregularities, and confirm proceedings which without the confirmation would be void, because unauthorized, provided such confirmation does not interfere with intervening rights.'

Here there has been an impermissible retroactive change in a legislative policy dating back to 1939. The Court below recognized and acknowledged that policy. (A13).

The action and intent of the 1939 Congress was clear, and the 1984 Congress cannot retroactively change longstanding Congressional policy.

There was no change in the 1939 Congressional intent to exclude these contributions from FICA taxation until the 1983 Social Security Amendments. The 1939 statute is controlling for the period at issue. Here, the 1984

Congress reached back to 1939 to change the prior Congress' intent to exclude these amounts from FICA taxation. This cannot be done.

Rowan teaches that absent Congressional intent to the contrary, there cannot be a difference in the treatment of the definition of wages for FICA purposes.

At the time that the claims for refunds were made and rejected (the rejection was dated April 30, 1984), the position of the Internal Revenue Service, based on Revenue Ruling 65-208, was wrong as a matter of law. The statute barring refunds did not become law until July 18, 1984. Petitioner would have been entitled to collect the refunds had Congress not later acted to attempt to bar them.

At the time that the I.R.S. rejected the refund claims it had absolutely no basis in law to do so. The government should be estopped from benefiting from its failure to follow established law. As of April 30, 1984 the law was that the monies paid were not ~~F~~.I.C.A. taxable. The taxpayer then had an absolute vested right to a refund both when the refund claim was made and on April 30, 1984 when I.R.S. rejected the claim.

In his Treatise of Civil Government and A Letter Concerning Toleration John Locke, in his essay "Of the Extent of the Legislative Power" (Meredith Publishing Company, 1965) at pages 92-93 wrote:

> For all the power the government has, being only for the good of the society, as it ought not to be arbitrary and

> at pleasure, so it ought to be exercised by established and promulgated laws; that both the people may know their duty and be safe and secure within the limits of the law; and the rulers too kept within their due bounds, and not be tempted by the power they have in their hands to employ it to such purposes, and by such measures as they would not have known, and own not willingly.

The 1984 Congress had no authority to retroactively change legislative policy which dated back to 1939. In Ogden v. Blackledge, 2 Cranch 272, 277, 2 L.Ed. 276, 278 (U.S. 1804), the Court stated:

> [T]o declare what the law is, or has been, is a judicial power; to declare what the law shall be, is legislative. One of the fundamental principles of all our governments is that the legislative power shall be separated from the judicial.

A current Congress cannot retroactively override prior Congressional

action and intent when that action and intent is clear and unambiguous, especially where the Supreme Court of the United States has already defined that prior Congressional intent. This Court must reverse the decision below because the Court below has done just that.

During the period at issue, Section 3121(a)(2) of the Code and its predecessor sections excluded payments made to Section 403(b) tax sheltered annuities from taxes under FICA. This evidenced a longstanding Congressional intent to exclude these payments and to encourage retirement savings. This section of the Code was not changed until the Social Security Amendments of 1983, supra. The definition of wages

was changed prospectively only, not retroactively.

The district court found that even though the 1984 amendments "do not, by themselves, apply to Canisius' claim that FICA taxes paid in 1980 should be refunded" (A51), the claims should be precluded because of Congressional intent to do so.

The circuit court stated ". . .the 1984 provision, by its literal terms, retroactively validates only taxes levied in conformity with regulations previously invalid under Rowan. However, we find the legislative intent so clear as to prevail." (A22).

Judge Weis answers this in Temple at 769 F.2d 139. He states:

> "This is contrary to what the Supreme Court said in Iselin v. United States, 270 U.S. 245, 251 (1926), -- the court

> should not enlarge a statute so that "what was omitted, presumably by inadvertence, may be included within its scope. To supply omissions transcends the judicial function."

Mr. Justice Felix Frankfurter stated "An omission, at the time of enactment, whether careless or calculated, cannot be judicially supplied however much later wisdom may recommend the inclusion." (Emphasis added.) "Some Reflections of the Reading of Statutes," 2 The Record of the Association of the Bar of the City of New York, 213, 222 (June 1947).

There is no basis in law for giving the statute words that the enacting Congress did not.

III. THIS COURT SHOULD GRANT CERTIORARI TO RESOLVE A CONFLICT IN THE CIRCUITS REGARDING THE WEIGHT TO BE GIVEN TO A REVENUE RULING.

This court should grant certiorari to resolve a conflict between the Third Circuit on the one hand and the First and Second Circuits on the other hand regarding the weight to be given to a revenue ruling when the express legislative history of the relevant statute is contrary to the revenue ruling.

The Temple Third Circuit majority relied upon Revenue Ruling 65-208 as its basis for interpreting the legislative history of the 1939 legislation to reach its conclusion that Section 3121 did not apply to contributions made to tax sheltered annuity plans funded through salary reduction agreements.

The Second Circuit in Canisius held that Revenue Ruling 65-208 was "in conflict not only with the plain language of the exclusion from FICA wages for the amount 'paid by an employer' but also with the interpretation accorded to the similar statutory language in Section 403(b)." (A17). In New England Baptist Hospital v. United States of America, [(No. 86-1540, slip op. (1st Cir. December 17, 1986)] the First Circuit agreed with the Canisius Court.

CONCLUSION

For the foregoing reasons, a writ of certiorari should issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit.

Respectfully submitted,

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January 16, 1987

APPENDIX

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 1429 August Term, 1985

(Argued June 10, 1986 Decided Aug. 20, 1986)

Docket No. 86-6065

CANISIUS COLLEGE,
Plaintiff-Appellant,
v.
UNITED STATES OF AMERICA,
Defendant-Appellee.

B e f o r e: WINTER AND PRATT, *Circuit Judges*, and MALETZ,* *Senior Judge*.

Appeal from an order of the United States District Court for the Western District of New York, John T. Elfvin, *Judge*, granting the government's motion for summary judgment in an action in which appellant Canisius College sought refund of certain FICA taxes.

Affirmed.

DAVID A. KAPELMAN, P.C., New York, New York, *for Plantiff-Appellant*.

*The Honorable Herbert N. Maletz, of the United States Court of International Trade, sitting by designation.

MICHAEL J. ROACH, U.S. Dept. of Justice, Tax Division, Washington, D.C., (Michael L. Paup and Jonathan S. Cohen, Washington, D.C., of counsel), *for Defendant-Appellee*

OPINION OF THE COURT

MALETZ, *Senior Judge*.

Appellant, Canisius College (Canisius) seeks a refund of employer and employee Federal Insurance Contributions Act (FICA) taxes paid by it and its employees for the 1980 tax year on amounts Canisius had contributed to employee retirement annuity contracts under a salary reduction plan. The United States District Court for the Western District of New York, John T. Elfvin, *Judge*, granted summary judgment for the government, holding that Canisius was not entitled to a refund. We affirm.

I. Introduction

The facts are not in dispute. Canisius is a nonprofit educational institution exempt from federal income tax under sections 501(a) and 501(c) (3) of the Internal Revenue Code of 1954, 26 U.S.C. §§ 501(a), 501(c)(3). As an organization described in section 501(c) (3), Canisius was qualified to establish an annuity plan for its employees under section 403(b) of the Code.[1] Canisius' type of section 403(b) plan is known as a "salary reduction" plan. Under that plan, employees desiring to purchase retirement annuity contracts entered into "salary reduction agreements" in which they agreed to accept salary reductions amounting to a specified percentage of their compensation, and Canisius, in exchange,

agreed to apply that amount toward the purchase of their retirement annuities.[2]

Under Treasury Department regulations, the amounts contribued by Canisius to retirement annuities in accordance with this salary reduction plan were considered contributions made by the employer for section 403(b) purposes and so were not taxable as gross income to the employees.[3] Those amounts were therefore not includable in employee "wages" for *income-tax withholding* purposes. Rev. Rul. 65-209, 1965-2 C.B. 414. However, in conformity with a 1965 revenue ruling, Rev. Rul. 65-208, 1965-2 C.B. 383, Canisius in 1980 included in "wages" for *FICA* tax purposes the amounts it had contributed under its salary reduction plan. On behalf of itself and certain of its

employees, Canisius filed this suit seeking a refund of the FICA taxes paid.

II. *Background*

We note at the outset that "wages" are the basis for determining employer obligations both for FICA and income-tax withholding purposes. 26 U.S.C. §§ 3101(a), 3111, 3402(a). The statutory definitions of "wages" for FICA and for income-tax withholding purposes are substantially identical in that each provides generally that wages constitute "all remuneration."[4] However, each definition contains various exclusions. As of 1980, the Code excluded from FICA wages:

> the amount of any payment (including any *amount paid by an employer for* insurance or *annuities*, or into a fund, to provide for any such payment)

> made to, or on behalf of, an employee or any of his dependents under a plan or system established by an employer which makes provision for his employess generally . . . *on account of*--
> (A) *retirement*. . . .

26 U.S.C. § 3121(a) (2) (emphasis added)

In 1965, the Internal Revenue Service ruled that the amounts paid by an employer for annuity contracts under a section 403(b) salary reduction plan -- as opposed to a salary supplement plan -- were includable in FICA wages. Rev. Rul. 65-208, 1965-2 C.B. 383 ("65-208"). The ruling specified that although such amounts were considered to be "contributed by the employer" and were therefore exempt from income tax under section 403(b), they were *not* to be considered as amounts "'paid by an employer' for an annuity contract" and hence *were* subject to FICA tax. In the

view of the Service, since the purposes of the section 403(b) income exclusion and of the FICA wage exclusion were "substantially different," the similar language in those statutes did not have to be similarly interpreted.

In 1981, in *Rowan Companies, Inc. v. United States*, 452 U.S. 247 (1981), the Supreme Court concluded that the language and legislative history of the relevant Acts indicated that Congress intended that the FICA and FUTA definitions of wages be interpreted in the same manner as the income-tax withholding definition of wages. *Id.* at 263. Consequently, the Court found invalid a Treasury regulation that required inclusion of the value of certain tax-exempt meals and lodging in FICA and FUTA wages although the same

value was not included in wages for income-tax withholding purposes.

The premise of *Rowan* -- that the Treasury Department must similarly interpret the similar definitions of wages -- cast doubt on the validity of 65-208, because that ruling required inclusion of amounts paid by employers for annuity contracts under salary reduction plans in FICA wages even though such amounts were not included in wages for income-tax withholding purposes.

In 1983, Congress partially codified the *Rowan* decision by amending the Social Security Act to provide that the value of the meals and lodging at issue in *Rowan* were not includable in FICA and FUTA wages. 26 U.S.C. § 3121(a) (19) (Supp. I 1983); *id.* § 3306(b) (14). However, Congress acted

to preclude the possible impact of *Rowan* on 65-208 by amending the definitions of FICA and FUTA wages. *See* S. Rep. No. 23, 98th Cong., 1st Sess. 41, *reprinted in* 1983 U.S. Code Cong. & Ad. News 143, 182 (amendments are intended to codify 65-208). Among other things, these amendments -- which became effective December 31, 1983[5] -- (1) deleted the statutory exclusion from FICA wages for amounts paid by employers for retirement plans, Social Security Amendments of 1983, Pub. L. No. 98-21, § 324(a)(3)(A), 97 Stat. 65, 123 ("1983 Act"), and (2) added a new subsection that excluded from FICA wages any employer payment

> under or to an annuity contract described in section 403(b), *other* than a payment for the purchase of such contract which is made by reason of a salary reduction agreement . . . .

26 U.S.C. § 3121(a) (5) (D) (Supp. II 1984) (formerly codified at 26 U.S.C. § 3121(a) (5) (E) (Supp. I 1983)) (emphasis added).

Additionally, Congress in 1983 overturned the general premise of *Rowan* by enacting provisions that "decoupled" the interpretations of FICA and FUTA wages from the interpretation of wages for income-tax purposes. The FICA "decoupling" clause applied to remuneration paid after December 31, 1983,[6] and provided:

> Nothing in the regulations prescribed for purposes of chapter 24 (relating to income tax withholding) which provides an exclusion from "wages" as used in such chapter shall be construed to require a similar exclusion from "wages" in the regulations prescribed for purposes of this [FICA] chapter.

26 U.S.C. § 3121(a) (Supp. I 1983).

This "decoupling" provision was enacted because of the congressional view that the objectives of the social security system differ from those of the income-tax withholding system, and that the Treasury Department should therefore be permitted to treat those systems differently. *See* S. Rep. No. 23, 98th Cong., 1st Sess. 42, *reprinted in* 1983 U.S. Code Cong. & Ad. News 143, 183.

In 1984, in the Deficit Reduction Act of that year, Congress altered the date on which the FICA "decoupling" provision of the 1983 Act was to become effective:

> *The amendments made by subsection (b)* . . . [the FICA "decoupling" provision] *shall apply* to remuneration . . . paid after March 4, 1983, and *to any such remuneration paid on or before such date which the employer treated as wages when paid.*

Pub. L. No. 98-369, § 2662(g), 98 Stat. 494, 1160 (emphasis added).

Against this background, the district court determined that 65-208 was invalid as of 1980 because it conflicted with the specific statutory exclusion from FICA wages of amounts "paid by an employer" for retirement annuities. *Canisius College v. United States*, No. 84-1126, slip op. at 5 (W.D.N.Y. Mar. 10, 1986). The court concluded, however, that 65-208 had been retroactively codified by the 1984 provision of the Deficit Reduction Act. *Id.* at 6-7. It therefore granted summary judgment for the government. This appeal by Canisius followed.

BEST AV

III. *Validity of 65-208*

We agree with the district court that 65-208 was invalid as of 1980 as contrary to the statutory exclusion from FICA wages.[7] We conclude also that even were the ruling not invalid on that ground, it was contrary to the *Rowan* requirement that "wages" be similarly interpreted for FICA and income-tax withholding purposes.[8]

A. *Validity under Statutory Exclusion*

We think it is clear that the payments made by Canisius under its salary reduction plan fall within the plain language of the exclusion from FICA wages, in effect during the tax year in issue, of amounts "*paid by an employer* for . . . annuities . . . under a plan . . . on account of . . . retirement." 26 U.S.C. § 3121(a) (2)

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(emphasis added). The amounts were not paid out of employee salaries. To the contrary, the employees had agreed to be paid less salary in the future, and, as consideration for those agreements, the amounts contributed for the annuities were to be paid out of Canisius' funds.

This conclusion that salary reduction plan payments are within the FICA wage exclusion is supported by the legislative history of the provision. That history indicates that the exclusion covered "*all* payments" made by the employer to or on behalf of an employee for retirement. H.R. Rep. No. 728, 76th Cong., 1st Sess., *reprinted in* 1939-2 C.B. 538, 548 (emphasis added). It further indicates that:

> These payments will be excluded *even though the amount or possibility of such payments is taken into consideration in fixing the amount of remuneration* and even though such payments are required, either expressly or impliedly, by the contract of employment.

Id. (emphasis added); *see* S. Rep. No. 734, 76th Cong., 1st Sess., *reprinted in* 1939-2 C.B. 565, 575-76.

> The reason for the exclusion was to save employers time and money but what is more important is that it will eliminate any reluctance on the part of the employer to establish such plans due to the additional tax cost.

H. Rep. No. 728, 76th Cong., 1st Sess., *reprinted in* 1939-2 C.B. 538, 543. The Social Security Board recommended to the Congress

> Exclusion from the definition of wages of all payments made by an employer to or on behalf of an employee under a plan or system providing for retirement benefits, dismissal

> wages, disability benefits, and medical and hospital expenses. The purpose of this proposal *is to avoid discouraging plans of the nature described.*

Social Security Board, Report Recommending Changes in the Social Security Act, H.R. Doc. No. 110, 76 Cong., 1st Sess. 12 (1939) (emphasis added).

Given the broad purpose manifested by this legislative history of encouraging employers to establish private retirement plans even at the expense of the FICA wage base, we think it follows that the wage exclusion was intended to cover payments made under salary reduction plans.

An additional factor impelling the conclusion that the FICA wage exclusion encompassed payments under section 403(b) salary reduction plans is that such payments are considered

"contributed by [the] employer" for purposes of section 403(b), and so are excludable from employee gross income. *See* 26 U.S.C. § 403(b); Treas. Reg. § 1.403(b)-1(b) (3), T.D. 6783, 29 Fed. Reg. 18,360 (1964). Revenue Ruling 65-208 was therefore in conflict not only with the plain language of the exclusion from FICA wages for the amount "paid by an employer" but also with the interpretation accorded to the similar statutory language in section 403(b).[9]

B. *Validity Under Rowan*

Even if 65-208 were to be viewed as not in conflict with a specific statutory exclusion from FICA wages, it would nonetheless be contrary to *Rowan*. For it included an amount in FICA wages that was *not* included in wages for income-tax withholding purposes and was

thus inconsistent with the *Rowan* requirement of parallel treatment of wages for FICA and income-tax purposes.

IV. *Retroactive Validation of Tax Paid Under 65-208*

We now consider whether FICA taxes paid in conformity with Revenue Ruling 65-208 were retroactively validated by Congress in 1984. Our discussion begins with the *1983* "decoupling" provision:

> Nothing in the regulations prescribed for purposes of chapter 24 (relating to income tax withholding) which provides an exclusion from "wages" as used in such chapter shall be construed to require a similar exclusion from "wages" in the regulations prescribed for purposes of this [FICA] chapter.

26 U.S.C. § 3121(a) (Supp. I 1983). By this provision it is apparent that Congress intended to overturn the underlying premise of *Rowan* by permitting the

Treasury Department to interpret the term "wages" differently for FICA and for income-tax withholding purposes, thereby validating prospectively regulations that had been invalid because of divergent interpretations.[10]

We next turn to the 1984 provision:

> The amendments made by subsection (b) . . . [the 1983 FICA "decoupling" provision] *shall apply* to remuneration . . . paid after March 4, 1983, and *to any such remuneration paid on or before such date which the employer treated as wages when paid.*

1984 Act § 2662(g) (emphasis added).

It is manifest that this 1984 provision makes the validating function of the 1983 "decoupling" clause retroactively applicable to "remuneration paid on or before [March 4, 1983] which the employer treated as wages when paid." And "remuneration . . . treated

as wages when paid" can only refer to remuneration that when paid was subject to taxation as "wages" pursuant to regulations previously unlawful under *Rowan*. So, the provision by its literal terms retroactively validates taxation previously unlawful because levied under regulations in conflict with *Rowan*.

The legislative history makes it clear, however, that Congress enacted the 1984 provision because of its concern as to the possible impact of *Rowan* on the validity of 65-208, and its concern that refunds of taxes paid in conformity with that ruling might be required:

> *If the 1965 revenue ruling [65-208] were determined to be invalid, then employers and employees would be eligible for refunds* for open years because taxable wages would be lower. In addition, wages for

> benefit computation purposes would be reduced, leading in some cases to reduction of social security benefits being paid to current beneficiaries and recoupment of a portion of benefits which have been paid in recent years on the basis of wage records which included the salary reduction contributions.

H.R. Rep. No. 432, 98th Cong., 2nd Sess., 1658, *reprinted in* 1984 U.S. Code Cong. & Ad. News 697, 1280 (emphasis added). Congress also wished to avoid the possibility that the originally prospective effective dates of the 1983 "decoupling" provisions

> could be cited as demonstrating Congressional intent that the reasoning of the *Rowan* decision should generally apply before these dates to types of remuneration other than meals and lodging . . . *e.g., to contributions under a salary reduction agreement to tax-sheltered annuities (sec. 403(b)).*

Id. (emphasis added). Thus, we think it evident that Congress intended to preclude the possibility of refunds of FICA taxes paid in conformity with 65-208 on amounts contributed under section 403(b) salary reduction plans.

As we have previously indicated, the 1984 provision, by its literal terms, retroactively validates only taxes levied in conformity with regulations previously invalid under *Rowan*. However, we find the legislative intent so clear as to prevail. Statutory language is ordinarily regarded as conclusive *"[a]bsent* a clearly expressed legislative intention to the contrary." *Consumer Product Safety Commission v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980) (emphasis added); *accord Dickerson v. New Banner Institute, Inc.*,

460 U.S. 103, 110 (1983) (same). The literal wording of a statute is "not the sole index to legislative intent. It cannot prevail over strong contrary indications in the legislative history . . . ." *Lange v. United States*, 443 F.2d 720, 722-23 (D.C. Cir. 1971) (footnote omitted); *accord Bob Jones University v. United States*, 461 U.S. 574, 586 (1983) (court should go beyond the literal language of statute if reliance on language would defeat plain purpose of statute); *In re Adamo*, 619 F.2d 216, 222 (2d Cir.) (court would not apply statute in accord with its literal meaning where that would pervert its manifest purpose), *cert. denied*, 449 U.S. 843 (1980); *In re Miracle Mart, Inc.*, 396 F.2d 62, 64 (2d Cir. 1968) (literal language of statute not relied

upon where congressional intent would be nullified). Here, the legislative history is "very clear . . . . [that] Congress intended, through the 1984 amendments, to *eliminate* the very type of refund sought in the instant case." *Temple University v. United States*, *supra*, 769 F.2d at 133 (emphasis in original).

In short, we conclude that the 1984 provision retroactively validated previously unlawful FICA taxes paid on amounts contributed under salary reduction plans in conformity with Revenue Ruling 65-208. We now consider whether such retroactive validation is constitutional.

V. *Constitutionality of Retroactive Tax*

Under *Welch v. Henry*, 305 U.S. 134, 147 (1938), a retroactive tax is

constitutional unless its application is so "harsh and oppressive" as to violate due process. This "harsh and oppressive" test does not differ from the test of constitutionality applicable to economic legislation generally, namely, that such legislation is constitutional unless Congress has acted in an arbitrary and irrational way. *Pension Benefit Guaranty Corp. v. R.A. Gray & Co.*, 467 U.S. 717, 733 (1984); *see Usery v. Turner Elkhorn Mining Co.*, 428 U.S. 1, 15 (1976). However, the retroactive application of the statute must be justified by a rational purpose. *Pension Benefit Guaranty Corp.*, 467 U.S. at 730; *Long Island Oil Products Co. v. Local 553 Pension Fund*, 775 f.2d 24, 27 (2d Cir. 1985) (retroactive statute is

constitutional if retroactive application is justified by legitimate legislative purpose furthered by rational means).

Among the factors to be considered in an assessment of whether a retroactive statute is harsh and oppressive in application is whether it abrogates vested rights. *See* Hochman, *The Supreme Court and the Constitutionality of Retroactive Legislation*, 73 Harv. L. Rev. 692, 696 (1960) (traditional principle used in assessing constitutionality of retroactive law is that statute may not abrogate vested rights, but term "vested rights" is conclusory -- a right is vested when so far perfected that it cannot be taken away by statute); *Patlex Corp. v. Mossinghoff*, 758 F.2d 594, 602 (Fed.

Cir.) (early Supreme Court cases concluded that retroactive statutes could not abolish property rights; later cases placed greater weight on policy considerations and established multifactor inquiry), *modified on other grounds*, 771 F.2d 480 (Fed. Cir. 1985). However, retroactive legislation is not unconstitutional merely because it upsets settled expectations or because it effectively imposes a new liability on a past act. *See Pension Benefit Guaranty Corp.*, 467 U.S. at 729-30; *Usery*, 428 U.S. at 16.

No vested right of Canisius was impaired by retroactive application of the 1984 provision. *Forbes Pioneer Boat Line v. Board of Commissioners*, 258 U.S. 338 (1922), relied upon by Canisius, is not to the contrary. In *Forbes*, the

plaintiff steamboat company had received a favorable final judgment in an action brought to recover tolls that had been unlawfully collected on passages through the lock of a canal. The state legislature enacted a law the day the judgment was issued purporting to retroactively validate the collection of tolls; the *Forbes* Court found the law unconstitutional. Canisius contends that the 1984 provision is similarly unconstitutional because it deprives Canisius of its right to a refund of FICA taxes. But Canisius, unlike the *Forbes* plaintiff, has no final judgment establishing such a right, nor does it have any other basis for claiming a vested right to such a refund. *See United States v. Heinszen & Co.*, 206 U.S. 370, 390-91 (1907) (Congress could

ratify admittedly unlawful collections of duties even after plaintiff had brought action to recover the duties paid); *Western Union Telegraph Co. v. Louisville & Nashville Railroad Co.*, 258 U.S. 13, 20 (1922) (where telegraph company had brought suit alleging right to easement under eminent domain statute, company did not have right so far vested under state law as to preclude change in statute that destroyed any such right of easement); *Taxpayers For The Animas-La Plata Referendum v. Animas-La Plata Water Conservancy District*, 739 F.2d 1472, 1477 (10th Cir. 1984) (Supreme Court has not hesitated to uphold legislation which has mooted pending lawsuits and nullified accrued causes of action).[11]

Another factor to be considered in assessing the constitutionality of a retroactive statute is whether the taxpayer relied on prior law so that, had he been able to foresee enactment of the legislation, he would have acted to avoid the tax. *See Usery*, 428 U.S. at 17 n.16; *Blodgett v. Holden*, 275 U.S. 142, 147 (1927) (it is wholly unreasonable that one who in good faith and without slightest premonition of such consequence made absolute disposition of property by gift should thereafter be required to pay charge for so doing), *modified on other grounds*, 276 U.S. 594 (1928); *Daughters of Miriam Center for the Aged v. Mathews*, 590 F.2d 1250, 1262 (3d Cir. 1978) (where retroactivity is challenged a critical question often is how conduct would have differed if rule

in issue had been applied from the start).

Here, the 1984 provision merely ratifies past action of the Treasury Department taken in conformity with long-standing department practice. Ruling 65-208 was promulgated in 1965, and nothing suggests that taxpayers, in planning employee benefit programs, relied on an assumption that amounts paid under salary reduction plans in 1980 would escape FICA taxation. *See Swayne & Hoyt, Ltd v. United States*, 300 U.S. 297, 302 (1937) (validating statute was constitutional where consequences of retroactive application were free of elements of novelty and surprise). Thus, there is no element of taxpayer reliance on prior law.

The length of the period affected is an additional factor to be considered in determining whether retroactive legislation is unduly harsh and oppressive in application. Retroactive tax law rarely concerns a time period longer than the year preceding passage of the legislation. *See United States v. Darusmont*, 449 U.S. 292, 296 (1981) (per curiam) (the retroactive feature of a tax statute usually has application only to the portion of current calendar year preceding date of its enactment). In the present case, the 1984 provision retroactively affects approximately a four-year period, from the 1980 tax year in issue, to the year of the provision's enactment. Despite the lengthy period affected, retroactive application of the provision is not impermissible. There

is nothing intrinsic in the "harsh and oppressive" test of *Welch v. Henry*, 305 U.S. at 147, or in the "arbitrary and irrational" test of *Usery*, 428 U.S. at 15, that requires a one-year bench mark as the constitutional limit of retroactivity. To the contrary, the nature of those tests, requiring that the court "[i]n each case . . . consider the nature of the tax and the circumstances in which it is laid," *Welch*, 305 at 147, suggests that the length of the period retroactively affected should be considered merely as a factor -- albeit a significant factor -- in the overall assessment of the constitutionality of the legislation.

In light of its curative purpose, we find the provision constitutional notwithstanding the long period of

retroactivity. Congress may ratify acts it could originally have authorized, *Swayne & Hoyt, Ltd. v. United States*, *supra*, 300 U.S. at 301-02, and curative legislation is typically entitled to be liberally construed, *Temple University*, *supra*, 769 F.2d at 134; 2 C. Sands, Sutherland Statutory Construction § 41.11 at 289-90 (4th ed. 1973). Congress' concern was that a failure to make retroactively lawful the taxes in issue, which had for years been collected in conformity with 65-208, would require refunds of monies that had provided a portion of the tax base of the social security system and necessitate some reduction of benefits to and recoupment of past benefits from current recipients. *See* H.R. Rep. No. 432, 98th Cong., 2d Sess. 1658, *reprinted in* 1984

U.S. Code Cong. & Ad. News 697, 1280-81. Considering the absence of either vested interests or taxpayer reliance, Congress' decision to address its concern by making retroactively lawful the taxes already collected is neither irrational, nor a harsh and oppressive way of "apportioning the cost of government among those who in some measure are privileged to enjoy its benefits and must bear its burdens," *Welch v. Henry*, 305 U.S. at 146. *Cf. Graham & Foster v. Goodcell*, 282 U.S. 409, 417-18, 426-29 (1931) (Court found constitutional retroactive statute designed to preclude necessity of refunding taxes that over three years earlier had been collected after limitations period had expired); *Rafferty v. Smith, Bell & Co.*, 257 U.S.

226, 231-32 (1921) (retroactive validation by Congress of duties unlawfully collected some four years earlier held constitutional).

In sum, because the retroactive application of the 1984 provision is curative in nature, rational in purpose, and not harsh or oppressive in result, the provision passes constitutional muster.

VI. *Conclusion*

For the reasons stated, we hold that Canisius is not entitled to a refund of the FICA taxes in issue.[12] We therefore affirm the district court's grant of summary judgment for the government.

FOOTNOTES

1. Section 403(b), 26 United States Code, provides in part:

> If . . . an annuity contract is purchased . . . for an employee by an employer described in section 501(c)(3) which is exempt from tax under section 501(a), ... and . . . the employee's rights under the contract are nonforfeitable, except for failure to pay future premiums, then amounts contributed by such employer for such annuity contract on or after such rights become nonforfeitable shall be excluded

from the gross income of the employee for the taxable year to the extent that the aggregate of such amounts does not exceed the exclusion allowance for such taxable year.

2. Another type of plan permissible under section 403(b) is a "salary supplement" plan under which an employer agrees that it will not only pay employees a certain salary, but that it will also contribute an additional amount to employee annuity contracts.

3. Employer contributions, under salary reduction plans or otherwise, are excluded from gross income only to the extent of an "exclusion allowance,"

which is generally twenty percent of an employee's includable income adjusted for certain other factors. 26 U.S.C. § 403(b); Treas. Reg. § 1.403(b)-1(b) (3), T.D. 6783, 29 Fed. Reg. 18,360 (1964).

4. More specifically, 26 U.S.C. § 3121(a), in the tax year in issue, provided that wages for FICA purposes are "all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash." 26 U.S.C. § 3401(a) provided that wages for purposes of income-tax withholding are "all remuneration (other than fees paid to a public official) for services peformed by an employee for his employer, including the cash value of all

remuneration paid in any medium other than cash."

"Wages are also the basis for determining employer obligations for Federal Unemployment Tax Act (FUTA) purposes. The general definition of FUTA wages is identical to the one for FICA wages. *See* 26 U.S.C. § 3306(b).

5. Social Security Amendments of 1983, § 324(d) (1), 97 Stat. 125.

6. 1983 Act, § 327(d) (1), 97 Stat. 127.

7. In this regard, our determination differs from that of the Third Circuit in *Temple University v. United States*, 769 F.2d 126, 129-30 (3d Cir. 1985),

cert. denied, 106 S. Ct. 2914 (1986). The court in *Temple* concluded that 65-208 was a correct interpretation of the statutory exclusion from FICA wages, which, in the court's view, did not encompass employer payments made under salary reduction plans. Our ultimate determination in this case is, however, in harmony with the decision in *Temple*.

8. It is to be noted that statutory interpretation as reflected in a revenue ruling does not have the force of law and is of little aid in interpreting a tax statute. *See Dixon v. United States*, 381 U.S. 68, 73 (1965); *Biddle v. Commissioner*, 302 U.S. 573, 582 (1938); *Temple University v. United States*, *supra*, 769 F.2d at 137 (Weis, J., dissenting).

9. As we have previously indicated, the rationale given in 65-208 itself for this discrepancy in the interpretation of the similar terminology in section 403(b) and in the FICA wage exclusion was that the "purposes of section 403(b) . . . and [of the FICA wage exclusion] are substantially different," and that therefore the fact that an amount was considered to be "contributed by the employer" for purposes of section 403(b) did not require a similar determination that it was an amount "paid by an employer" for purposes of the FICA wage exclusion. This rationale closely resembles that found invalid in *Rowan* and so is clearly inadequate to sustain a conclusion that, *as of 1980*, 65-208 constituted a proper interpretation of

original legislative intent regarding the specific statutory exclusion from FICA wages for amounts "paid by an employer" for annuities.

10. The legislative history of the provision indicates that Congress intended to address both Treasury Department regulations and revenue rulings. *See* S. Rep. no. 23, 98th Cong., 1st Sess. 42, *reprinted in* 1983 U.S. Code Cong. & Ad. News 143, 183 (determination of whether amounts are to be included in social security wage base is to be made without regard to whether the amounts are treated as wages for income-tax withholding). Consequently, references hereafter to "regulations" also refer to revenue rulings.

11. Canisius' argument that the 1984 provision violates the constitutional doctrine of separation of powers by "retroactively overruling" the *Rowan* decision is without merit.

The 1984 provision did not impair the judgment in *Rowan* -- indeed, as previously noted, Congress codified the specific *Rowan* decision. Nor was the 1984 provision intended to affect the rights of a litigant in a particular case. *See Temple University v. United States*, 769 F.2d at 134 n.4 (Congress by the 1984 provision did not violate separation of powers doctrine); *cf. Hurtado v. California*, 110 U.S. 516, 535-36 (1884) (law must not be special rule for particular person or particular case).

12. The Third Circuit and several district courts have held to the same effect. *See Temple University v. United States, supra*, 769 F.2d 126; *University Health Center, Inc. v. United States*, 622 F. Supp. 88 (D. Vt.), *appeal dismissed* No. 85-6340 (2d Cir. Dec. 31, 1985); *Xavier University v. United States*, 633 F. Supp. 15 (S.D. Ohio), *appeal pending*, No. 86-3328 (6th Cir. 1986); *New England Baptist Hospital v. United States*, 634 F. Supp. 810 (D. Mass. 1986).

UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NEW YORK

CANISIUS COLLEGE,

Plaintiff,

—vs—

UNITED STATES OF AMERICA,

Defendant.

CIV-84-1126E

MEMORANDUM and ORDER

The plaintiff ("Canisius") seeks a refund of Federal Insurance Contribution Act ("FICA") contributions made in 1980 and the defendant has moved and the plaintiff has cross moved for summary judgment.

The facts are not in dispute. Canisius is a non-profit educational institution exempt from federal income tax pursuant to section 501(c)(3) of the Internal Revenue Code. In 1980 Canisius had in effect an employee retirement annuity plan of a type described in 26 U.S.C. §403(b). Under such plan certain employees agreed to accept wage reductions in exchange for Canisius's purchase of annuity contracts on their behalves. Pursuant to section 403(b), the cost or value of the contracts was excludable from the employees' 1980 gross income for federal withholding tax purposes. No question appears to exist concerning Canisius's eligibility to develop or implement such a plan or concerning the propriety of excluding the cost or value of the annuities from the participating employees' gross income for federal income tax withholding purposes.

In contrast to the treatment of such employer contributions for income tax purposes, the amounts used to purchase annuities had been declared in Revenue Ruling 65-208, 1965-2 Cum. Bull. 383, to be includable in the FICA wage base. In compliance with such ruling, Canisius withheld taxes from its employees' wages based upon such inclusion. Canisius also paid the corresponding FICA taxes imposed on it as an employer as measured by the FICA taxable wage bases of its employees.

In 1981 the United States Supreme Court decided *Rowan Cos. v. United States* ("*Rowan*"), 452 U.S. 247, which held that "wages" must be consistently interpreted for federal income withholding and for FICA purposes. *Id.* at 263.

In light of such holding, Canisius sought the refund of employer and employee FICA taxes for the 1980 tax year together with statutory interest on behalf of itself and a number of its employees who had participated in the salary reduction annuity plan. In a letter dated April 30, 1984 the Director of the Massachusetts Service Center of the Internal Revenue Service notified Canisius that the refund request had been disallowed in full based upon Revenue Ruling 65-208.

Canisius alleges in this action that "wages" subject to FICA taxation, despite Revenue Ruling 65-208, at all times excluded the payments made for retirement annuities. 26 U.S.C. §3121(a), promulgated in 1939, defines "wages" subject to FICA taxes. That subsection, as it existed during the 1980 tax year at issue in this action, included as wages

> "all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash ***."

The statute excluded from the definition of wages

> "the amount of any payment (including the amount paid by an employer for insurance or annuities, or into a fund, to provide for any such payment) made to, or on behalf of, an employee or any of his dependents

> under a plan or system established by an employer which makes provision for his employees generally *** on account of — (A) retirement ***." 26 U.S.C. §3121(a)(2).

The definition of wages for federal income tax withholding purposes is almost identical to that used to define wages for FICA purposes. *See Rowan, supra*, at 255. Section 403(b), using language very similar to that used in subsection 3121(a)(2), provides the basis for excluding under particular circumstances the value of an employer purchased annuity from an employee's federal income tax wage base.[1] Section 403(b) has been held to exclude from the federal income tax wage base both amounts contributed by an employer in addition to an employee's regular salary and amounts contributed in lieu of the employee's salary pursuant to a salary reduction plan. *See Temple University v. United States*, 769 F.2d 126, 133 (3rd Cir. 1985). Despite the similarity between sections 403(b) and 3121(a)(2), Revenue Ruling 65-208 held that the latter excluded from the FICA wage base only salary supplements used to purchase retirement annuities and not salary reduction amounts used to purchase such annuities.

As in the court of appeals decision in *Rowan* it is possible to rationalize the disparate treatment given salary reduction and retirement annuity purchase plans under the federal withholding and FICA schemes if one looks to the different purposes of FICA and federal income tax. A lesson of *Rowan*, however, is that, absent express congressional intent to the contrary, the term wages is to be interpreted in the same manner for FICA purposes as for income tax withholding purposes. Nevertheless and despite

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[1] Section 403(b) provided that, if an annuity contract is purchased for an employee by an employer described in section 501(c)(3) which is exempt from tax under secton 501(a) and the employee's rights under the contract are nonforfeitable except for failure to pay future premiums, then amounts contributed by such employer for such annuity contract on or after such rights become nonforfeitable shall be excluded from the gross income of the employee for the taxable year to the extent that the aggregate of such amounts does not exceed the exclusion allowance for such taxable year.

the language used in *Rowan*, the present action may be distinguished on the basis that the federal income tax statute at issue in *Rowan* excluded certain income from taxable wages and it was found that such exclusion was reflected in the FICA wage base calculation. Here, the federal income tax statute involved merely defers federal income tax liability and such deferment cannot be reflected under the present FICA scheme. The definition of FICA wages, unlike the federal income tax withholding definition of wages, does not include the value of annuity disbursements. This Court finds, however, that it is not called upon to decide whether the holding in *Rowan* requires that the definition of wages applied in deferring taxes on income produced by an employer's purchase of annuities must be applied to the definition of FICA wages.

In *Rowan* the question was the validity of a Treasury regulation. In the case at bar, this Court must initially focus on the validity of a revenue ruling. Although a Treasury regulation merits greater deference from a court, a revenue ruling is entitled to substantial deference and has "the force of legal precedents unless unreasonable or inconsistent with the provisions of the Internal Revenue Code." *Dunn v. United States*, 468 F.Supp. 991, 993 (S.D.N.Y. 1979). In evaluating the reasonableness of a regulaton or ruling, a court must determine whether it "harmonizes with the plain language of the statute, its origin, and its purpose." *See Rowan, supra*, at 253, *quoting from National Muffler Dealers Assn. v. United States*, 440 U.S. 472, 477 (1979).

The plain language of section 3121(a)(2) made no distinction between wage supplement and wage reduction amounts used by an employer to purchase annuities on account of an employee's retirement. As is noted in Judge Weis's dissent in *Temple University v. United States*, *supra* at 126, 136-137, the legislative history of the section and the administrative application of the section demonstrate that no distinction had been made between supplemental and reduction amounts until 1965. Only upon the emergence of concern for the stability of the FICA wage base was this contrary ruling promulgated. Although the ruling has been consistently interpreted since its publication, that consistency

and Congressional reliance upon its validity do not themselves serve to justify its unreasonable interpretation of the statute. This Court agrees that it is inappropriate to attempt to legitimatize Revenue Ruling 65-208 based upon the financial state of the national system of social insurance in 1965, 1983 or 1984 or upon Congress's 1983 and 1984 debates, reports and enactments amending the relevant law. It is therefore found that Revenue Ruling 65-208 did not validly reflect the plain language, origin or purpose of section 3121(a).

In 1983, however, apparently spurred by the decision in *Rowan*, Congress enacted the Social Security Amendments Act of 1983, ("the 1983 Act"), Pub.L. No. 98-21, 97 Stat. 65. The 1983 Act made two relevant changes to section 3121(a). It deleted the reference to "retirement" plans in the list of exclusions from the FICA wage base in the section and added subsection 3121(a)(5)(E)[2] which excludes from the FICA wage base any employer payment

> "under or to an annuity contract described in section 403(b), other than a payment for the purchase of such contract which is made by reason of a salary reduction agreement ***."

The 1983 Act, in effect, codified Revenue Ruling 65-208. Section 327(b) of the 1983 Act also added, after what is now 26 U.S.C. §3121(a)(20), a sentence which states that:

> "Nothing in the regulations prescribed for purposes of chapter 24 (relating to income tax withholding) which provides an exclusion from 'wages' as used in such chapter shall be construed to require a similar exclusion from 'wages' in the regulations prescribed for purposes of this chapter."

The sentence appears to serve to counteract the *Rowan* decision by expressly decoupling the FICA and federal withholding tax definitions of wages.

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[2] Now codified as 26 U.S.C. §3121(a)(5)(D).

The 1983 Act leaves no doubt that the type of claim presently before this Court was to be foreclosed. The amendments went into effect on January 1, 1984 and thus do not, by themselves, apply to Canisius's claim that FICA taxes paid in 1980 should be refunded.

In the Deficit Reduction Act of 1984 ("the 1984 Act"), Pub.L. No. 98-369, 98 Stat. 494, Congress changed the effective date of section 327(b) of the 1983 Act. It made the FICA and federal income tax wage definition decoupling provision applicable to

> "remuneration *** paid after March 4, 1983, and to any such remuneration paid on or before such date which the employer treated as wages when paid." *Id.*, §2662(g).

The 1984 Act, however, did not expressly provide that the 1983 amendments to section 3121(a)'s definitions of wages were to be applied retroactively.

As noted in *Temple University v. United States*, *supra*, the legislative history of the 1984 Act reveals that it clearly had been Congress's purpose to foreclose the granting of refunds in cases such as the one presently before this Court. Despite the fact that the 1984 Act failed to make the 1983 Act's definition of the FICA wage base under section 3121(a) expressly retroactive to 1980, this Court finds that it serves to preclude the refund sought here. *Id.* at 132-133. The 1984 Act, therefore, had the effect of making the value or cost of employer purchased retirement annuities in this action taxable as part of an employee's FICA wage base.

Canisius alleges that the retroactive effect of the 1983 Act and the 1984 Act unconstitutionally overruled *Rowan*. That case however, did not, as Canisius contends, invalidate Revenue Ruling 65-208. As noted above, even after *Rowan*, a substantial question remained whether the reasoning in that decision provided a basis upon which to invalidate the distinction made between sections 403(b) and 3121(a)(2). In 1983 and 1984, Congress acted to codify the distinction before the question was answered. The amendments, therefore, did not unconstitutionally overrule *Rowan*.

Canisius also claims that the retroactive force of the 1983 Act and the 1984 Act violate the due process clause of the Fifth Amendment. As it notes, the United States Supreme Court has states that in cases such as this one "it is necessary to consider the nature of the tax and the circumstances in which it was laid before it can be said that its retroactive application is so harsh and oppressive as to transgress the constitutional limitation." *Welch v. Henry*, 305 U.S. 134, 147 (1938). Neither the highest court nor any intermediate federal court has adopted an absolute time limit on retroactivity. *Temple University v. United States*, *supra* at 135. Instead, a test for determining whether the retroactive application is so harsh, arbitrary or unfair so as to violate due process rights is "whether this taxpayer has had its expectations as to taxation unreasonably disappointed." *Wilgard Realty Co. v. Commissioner of Internal Rev.*, 127 F.2d 514, 517 (2d Cir., 1942). It was additionally noted therein that "retroactive taxation is not so arbitrary and oppressive as to be unconstitutional if it is no more burdensome than the taxpayer should have expected it to be when he did the thing which created the tax liablility" and that "when it is not, whether the period of retroactivity is comparatively long or short is of little consequence provided it isn't too long to be within reason." *Ibid.* The standard of oppressiveness is thus one of degree.

The five-year retroactive period in this case is relatively long. *See Welch v. Henry, supra; United States v. Hudson*, 299 U.S. 498, 501 (1937); *Purvis v. United States*, 501 F.2d 311 (9th Cir. 1974), *cert. denied* 420 U.S. 947 (1975); *Wilgard Realty Co. v. Commissioner of Internal Rev., supra*. A number of other factors convince this Court, however, that Canisius's due process rights had not been violated. Revenue Ruling 65-208 had been consistently applied since its publication in 1965 to include salary reduction amounts as wages and Canisius had complied with that ruling's interpretation of section 3121(a)(2) through the 1980 tax year. Its expectations would reasonably include the continued validity of the ruling. The decision in *Rowan*, while perhaps marginally changing Canisius's expectations, did not provide it with any certain right to a FICA tax refund. In addition, the 1983 Act and the 1984 Act were merely curative in the sense that

they sought to foreclose the possibility that *Rowan* would affect the rationale and effectiveness of Revenue Ruling 65-208. These factors persuade this court that the retroactive legislation did not unreasonably disappoint Canisius's expectations as to its FICA tax liability. The legislation, therefore, was not so oppressive so as to violate its due process rights.

Accordingly, it is hereby ORDERED that Canisius's motion for summary judgment is denied and that the defendant's motion for summary judgment is granted.

Dated: Buffalo, N.Y.
February 28, 1986

s/ John T. Elfvin
U.S.D.J.

Supreme Court of the United States

No. A-344

CANISIUS COLLEGE,

Applicant,

v.

UNITED STATES

ORDER EXTENDING TIME TO FILE PETITION FOR WRIT OF CERTIORARI

UPON CONSIDERATION of the application of counsel for the applicant,

IT IS ORDERED that the time for filing a petition for a writ of certiorari in the above-entitled case be, and the same is hereby, extended to and including January 17, 1987.

/s/ Thurgood Marshall
Associate Justice of the Supreme Court of the United States

Dated this 6th
day of November, 1986.

UNITED STATES COURT OF APPEALS

for the

SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the twentieth day of August one thousand nine hundred and and eighty-six

Present: HON. RALPH K. WINTER,

HON. GEORGE C. PRATT,

CIRCUIT JUDGES,

HON. HERBERT N. MALETZ,*

SENIOR JUDGE, USCIT

CANISIUS COLLEGE, Plaintiff-Appellant, -V- UNITED STATES OF AMERICA, Defendant-Appellee.	Docket No. 86-6065

Appeal from the United States District Court for the Western District of New York

This Cause came on to be heard on the transcript of record from the United States District Court for the Western District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged and decreed that the order of said District Court be and it hereby is affirmed in accordance with the opinion of this court with costs to be taxed against the appellant.

ELAINE B. GOLDSMITH,
Clerk

By: /s/Edward J. Guardaro,
Deputy Clerk

*The Honorable Herbert N. Maletz, of the United States Court of International Trade, sitting by designation.

UNITED STATES DISTRICT COURT

Western District of New York

JUDGMENT IN A CIVIL CASE

CASE NUMBER: Civil 84-1126E

CANISIUS COLLEGE,

V.

UNITED STATES OF AMERICA,

[ ] Jury Verdict. This action came before the Court for a trial by jury. The issues have been tried and the jury has rendered its verdict.

[X] Decision by Court. This action came to hearing before the Court. The issues have been heard and a decision has been rendered.

IT IS ORDERED AND ADJUDGED

That Canisius's motion for summary judgment is denied and that the defendant's motion for summary judgment is granted.

March 11, 1986 /s/Edward P. Gueth, Jr.
Date *Clerk*

(Also Section 403; 1.403(b)-1.) Rev. Rul. 65-208

An organization, described in section 501(c)(3) of the Internal Revenue Code of 1954 and exempt from income tax under section 501(a) of the Code, established a supplemental annuity plan for the benefit of its employees. Under the plan, an employee entered into an agreement to take a reduction in salary for the purpose of providing funds for the purchase of a nontransferable annuity contract on his behalf. The agreement applies only to amounts earned by the employee subsequent to the effective date of the agreement. The employee is not permitted to make more than one such agreement during any one taxable year. *Held*, under these circumstances, the amounts used pursuant to the salary reduction agreement to purchase the annuity contract are "wages" for purposes of section 3121(a)(2) of the Federal Insurance Contributions Act, even though such amounts, within prescribed limits, are excludable from the employee's gross income for purposes of section 403(b) of the Code, and are not subject to the withholding of income tax.

Revenue Ruling 181, C.B. 1953-2, 111, distinguished.

Advice has been requested whether, under the circumstances described below, amounts used by an exempt organization to purchase an annuity contract for one of its employees are "wages" for purposes of the Federal Insurance Contributions Act (Chapter 21, subtitle C, Internal Revenue Code of 1954).

An organization, described in section 501(c)(3) of the Internal Revenue Code and exempt from income tax under section 501(a) of the Code, established a supplemental annuity plan for the benefit of its employees. Under the plan, an employee entered into an agreement with the organization to take a reduction in salary for the purpose of providing funds for the purchase of a nontransferable annuity contract on his behalf. The agreement applies only to amounts earned by the employee subsequent to the effective date of the agreement. The employee is not permitted to make more than one such agreement during any one taxable year.

For purposes of this determination, it is assumed that the purchase of the annuity contract under the circumstances described above meets the requirements of section 403(b) of the Code. Therefore, amounts used to purchase the annuity contract, within the prescribed limits are excluded from the employee's gross income under that section of the Code for the taxable year contributed.

The term "wages", as defined in section 3121(a) of the Federal Insurance Contributions Act, means all remuneration for employment, including the cash value of all remuneration paid in any medium other than cash, with certain exclusions. The exclusion pertinent here is contained in section 3121(a)(2) of the Act, which provides, in part, that the term "wages" shall not include the amount of any payment (including any amount paid by an employer for insurance or annuities, or into a fund, to provide for any such payment) made to, or on behalf of, an employee or any of his dependents under a plan or system established by an employer which makes provision for his employees generally on account of retirement.

The question involved here is whether amounts "paid by an employer" for an annuity contract on behalf of an employee must be given the same treatment for purposes of both section 403(b) of the Code and section 3121(a)(2) of the Federal Insurance Contributions Act.

The purposes of section 403(b) of the Code and section 3121(a)(2) of the Federal Insurance Contributions Act are substantially different. Therefore, a determination under section 403(b) of the Code that a particular amount is "contributed by the employer" for the purchase of an annuity contract for an employee does not necessarily require a similar determination that it is also an amount "paid by an employer" under section 3121(a)(2) of the Federal Insurance Contributions Act.

Accordingly, it is held that, under the circumstances described herein, the amounts used by the organization pursuant to the salary reduction agreement to purchase the annuity for the employee are "wages" for purposes of the Federal Insurance

Contributions Act, even though such amounts, within prescribed limits, are excludable from the employee's gross income for purposes of section 403(b) of the Code.

However, the withholding of income tax is not required on such amounts used by the organization to purchase the annuity contract on behalf of the employee. See Rev. Rul. 65-209, page 414 this Bulletin.

The instant case is factually distinguishable from Revenue Ruling 181, C.B. 1953-2, 111, which holds, in effect, that an amount paid by an exempt organization as a premium for the purchase of an annuity contract on behalf of an employee does not fall within the meaning of the term "wages" as defined by the Federal Insurance Contributions Act. That Revenue Ruling contemplates a situation where an organization uses its own funds for the purchase of an annuity contract, rather than one where the employee takes a voluntary reduction in salary to provide the necessary funds.

Revenue Ruling 181, C.B. 1953-2, 111, is hereby distinguished.